IN THE

Supreme Court of the United States

OCTOBER TERM, 1979

No. 79-242

THE FRANKLIN LIFE INSURANCE COMPANY, A CORPORATION, INDIVIDUALLY AND REPRESENTATIVELY ON BEHALF OF ALL HOLDERS OF THE 9.44% CUMULATIVE PRIOR PREFERRED STOCK OF COMMONWEALTH EDISON COMPANY, A CORPORATION, *Petitioners,*

vs.

COMMONWEALTH EDISON COMPANY, A CORPORATION, *Respondent.*

BRIEF IN OPPOSITION TO PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE SEVENTH CIRCUIT.

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RESPONDENT'S BRIEF IN OPPOSITION TO PETITION FOR WRIT OF CERTIORARI.

The respondent, Commonwealth Edison Company ("Edison"), an Illinois public utility, respectfully requests that this Court deny the petition for a writ of certiorari seeking review of the decision of the Court of Appeals for the Seventh Circuit.

OPINIONS BELOW.

The *per curiam* opinion of the Court of Appeals, adopting the District Court's memorandum opinion, and the memorandum opinion itself are reproduced in the appendix to the petition.*

* Reference to those opinions will be made to the petition as "App. ....."

STATEMENT OF THE CASE.

This case concerns preferred shares of Edison stock (the "stock") sold by Edison at $100 per share in 1970 and redeemed by it at $110 per share in 1972. The gist of petitioner's suit is that Edison, under the terms of the stock issuance, did not have the right to redeem the stock in 1972, and therefore, that the redemption violated petitioner's common law contract rights and federal securities laws rights.

The argument which follows is essentially that the case did not, and cannot, turn on the questions raised now in the petition. For that reason, and because respondent's argument is brief, we do not attempt to restate the questions presented by petitioner. Instead, the questions actually decided by the District Court, along with some facts not contained in petitioner's statement of the case, are recited in the body of the argument.

REASONS FOR DENYING THE WRIT.

This is an action for an alleged breach of contract. Because the contract was for the purchase of a security, the suit, like many others in recent years, was filed in a federal court, claiming that the alleged breach was also a fraud under the securities laws.

The District Court found no breach and no securities fraud. The decision was affirmed *per curiam* by the Court of Appeals.

The case involves no conflict among circuits, nor novel interpretations of law. The federal questions which petitioner claims are raised, while perhaps interesting, were not decided below. They were not decided because the trial court, as to each question, assumed that the law was as the petitioner claimed, and then found that even under petitioner's theories the facts did not support liability. The two decisions below thus turned on findings of fact regarding the defendant's state of mind and the scope of the dissemination of certain information to the

public. As a result, the judgment can be reversed only by upsetting the trial court's findings of fact, as concurred in by the Court of Appeals, a result rarely achieved under the "two court rule". *Graver Tank & Mfg. Co.* v. *Linde Co.*, 336 U. S. 271, 275 (1949); *Berenyi* v. *Immigration Director*, 385 U. S. 630, 635 (1967).

The Petition suggests three federal legal issues as a basis for granting the writ: (1) the scope of the disclosure obligation imposed by the 1933 Act as it applies to the redemption terms of preferred stock; (2) the scope of the scienter standard established in *Ernst & Ernst* v. *Hochfelder*, 425 U. S. 185 (1976); and (3) whether a redemption is a "sale" for purposes of Section 10 of the 1934 Act or Section 17 of the 1933 Act. (Pet. at 12-13.) As a fourth basis, petitioner suggests review is in order simply because a large sum of money is involved (Pet. at 13.)

In fact, none of the bases—legal or monetary—are presented by the decisions below.

A. Economic Issue.

Petitioner's basic theory, in both the securities and contract branches of the case, was that Edison, like all large electric utilities, would be borrowing substantial amounts of money over the period from 1970 to 1980 to pay for new generating units. From the fact that Edison, as a "net borrower" over this period, knew that it would be selling new debt, petitioner surmised that Edison would therefore always be "in anticipation of the incurring of any debt . . ." as that phrase was used in the restriction on refunding. Thus Edison would never be able to redeem the stock. The problem, as the record below shows, was that petitioner confused economic reality with legal requirement. The actual effect of the large construction budgets was that most utilities needed every cent they could raise to pay their debts, and could not allocate newly raised funds to non-

operating purposes such as the redemption of earlier securities. Edison, for a time in 1972, happened to be able to afford that luxury. Its redemption, therefore, disappointed petitioner's economic expectation; that disappointment was then converted to a claim of legal wrong.

The record below included testimony regarding a large number of issues of utility preferred stock. That testimony (embodied in the District Court's opinion at App. 17 but not set out as detailed findings of fact) was that preferred stock is issued with a variety of terms relating to its redemption. Some allow redemption without restriction; some expressly prohibit redemption by saying that they are "not callable"; and some fall between those extremes. (Tr. 558-561.) That middle ground is itself of some width, and includes a variety of restrictions, both as to sources of funds that can or cannot be used, and as to the length of time and penalty price to be paid during the term of the restriction. (Tr. 561-563).

Nine of the preferred stock issues considered below contained no restrictions at all on redemption. All nine of those stocks were still outstanding at the time of trial in 1977. (Tr. 558-559.) The reason they are still out, as the testimony below established, was that redemption depends on the economic facts facing each company. Even without legal restrictions, preferred can be redeemed only if a company can afford to spend its funds to do so. In Edison's case, its 1970 preferred shares could be redeemed only if it could afford to sell common stock for that purpose. (Tr. 602-603.) While it is outside the record in this case, the price at which Edison can sell common shares is no longer above the book value of those shares. The same fact is true of almost all utilities.

While the case involves a fairly large sum, and other preferred issues of substantial size are in the hands of investors, the record below shows that this case will not decide the fate of other issues of preferred stock. The trial judge exercised care to confine his holdings to determinations on the facts of this

case. There is no holding suggesting a new or different standard for future financings. Additionally, petitioner's own argument has emphasized that Edison's redemption language, although "similar to that of other utilities," was used by no other utility. (Pet. at 22.) While some other utilities do in fact use this language, the record below reflects the large number of variants in use. The trial court's interpretation of particular language is scant cause to fear mass utility redemptions of preferred stock. The likelihood that any utility will be redeeming preferred shares, no matter what happens to this case, thus appears to be quite small.

The record thus tends to show that the risk which is said to justify granting certiorari here, that some billions of dollars of preferred shares will be redeemed if this case were affirmed, is a risk which can safely be left to the distinct economic and legal restrictions which were bargained into other issues of preferred shares.

B. Legal Issues.

The legal questions which petitioner seeks to raise are not presented by the opinions below.

The first legal issue raised by petitioner is whether the prospectus adequately described the redemption terms of the preferred shares. However, this is an issue that was not decided below because the case was disposed of on other grounds. The trial court reasoned that:

> Further, whether the language of the prospectus adequately disclosed these facts is another question on which I express no opinion.
>
> Assuming however, that the securities laws require this type of disclosure and that the prospectus did not adequately discloses these facts, the question remains whether the non-disclosure was done intentionally or recklessly or as part of a scheme or artifice to defraud. (App. 16.)

Issues which the trial court has expressly reserved as unnecessary to the decision are not proper basis for granting a writ of certiorari.

Petitioner's second legal issue is whether the court properly interpreted the scienter requirement of *Ernst & Ernst* v. *Hochfelder*, 425 U. S. 185 (1976), especially in light of petitioner's contention that recklessness may be sufficient basis for liability. The short answer to petitioner's question is that the trial judge ruled that petitioner had proven neither scienter nor recklessness in its case. (App. at 17.) No facts were found which could support liability under either standard. Petitioner's scienter issue is nonexistent.

Petitioner's final legal argument for granting the writ is that the antifraud provisions of the 1933 and 1934 Acts ought to apply to a redemption. The trial court did, however, "apply" the relevant antifraud provisions of those statutes to the redemption. (App. at 17-21.) The trial court went so far as to assume that there could be liability under Rule 10b-5, despite a wholly accurate registration statement, if Edison failed to timely inform the market of its intention to redeem. Under this most favorable interpretation of law for petitioner, the Court found that Edison had informed the market in a timely and adequate way, by sending proxy materials and a report of what occurred at its annual meeting to 190,000 shareholders, 1,134 brokers and analysts, and 260 newspapers. (App. at 20.) We do not know how to phrase a legal position more favorable to the petitioner than that applied by the trial court's analysis.

In sum, the legal issues on which petitioner seeks to justify its petition are simply not part of the controversy resolved below and, therefore, merit no consideration here.

C. Other Issues.

The petition also attempts to raise two common law contract questions. The first issue is whether Edison breached any contract it had with purchasers of the shares. The second is

whether Edison breached any contract it had with the New York Stock Exchange as to which some purchasers of the stock may have been third-party beneficiaries.

The common law principles of contract law which apply to each of these issues are well settled and apparently uncontested in the petition. Thus, there is no need for review of these matters by this Court.

The petition actually seeks a *de novo* review of the essentially factual determinations made by the trial court. Such a review is, of course, contrary to the generally applicable standard that factual determinations will be reversed only if clearly erroneous. *Roemer* v. *Maryland Public Works Bd.*, 426 U. S. 736, 758 (1976).

More importantly, in the absence of exceptional circumstances, mere factual questions are not proper objects of this Court's discretionary review powers. Petitioner points to no overriding consideration of public policy or issue of national import which would justify this Court injecting itself into essentially factual questions that have been thoroughly heard and identically decided by two separate tribunals.

CONCLUSION.

Petitioner has presented nothing to this Court which either generally conforms to the guidelines for granting certiorari set forth in Supreme Court Rule 19 or which otherwise demonstrates sufficient merit to require decision by this Court. The legal issues raised are not, in fact, in controversy here. Petitioner really seeks only a third chance to argue factual theories already twice rejected. For these reasons, the petition should be denied.

Respectfully submitted,

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